

Message Text

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ACTION NEA-10

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E.O. 11652: N/A
TAGS: ECON, IN
SUBJECT: THE INDIAN ECONOMY IN 1978-79

1. SUMMARY. INDIA'S ECONOMIC PERFORMANCE IN IFY 1978-79
MAY TURN OUT TO BE RELATIVELY GOOD, ALTHOUGH GROWTH IN GDP
WILL PROBABLY BE MODEST IN COMPARISON WITH THE ESTIMATED
6-7 PERCENT INCREASE IN GDP LAST FISCAL YEAR. THE MAJOR
ECONOMIC FACTOR IS THE FAVORABLE SOUTHWEST MONSOON SO FAR
THIS SUMMER, WHICH MAY RESULT IN A RECORD KHARIF (FALL)
HARVEST AND VERY SATISFACTORY FOODGRAIN PRODUCTION THIS
CROP YEAR. ON THE OTHER HAND, THE INDUSTRIAL SECTOR IS
STILL CONSTRAINED BY A NUMBER OF PROBLEMS, AND INDUSTRIAL
OUTPUT IS UNLIKELY TO REACH THE OFFICIAL GROWTH TARGET OF
7-8 PERCENT IN 1978-79. PRICES HAVE BEEN RELATIVELY
STABLE IN RECENT MONTHS BECAUSE OF AMPLE SUPPLIES OF
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ESSENTIAL COMMODITIES. A CONSIDERABLY LARGER TRADE
DEFICIT OF OVER \$1 BILLION IS EXPECTED THIS YEAR BECAUSE
OF RISING IMPORTS AND CONTINUED SLUGGISH EXPORT GROWTH,
BUT SIZEABLE FOREIGN EXCHANGE EARNINGS FROM TOURISM,
FOREIGN INVESTMENT AND, IN PARTICULAR, REMITTANCES FROM
INDIAN WORKERS IN THE MIDDLE EAST WILL HELP BRING ABOUT
A FAVORABLE BALANCE OF PAYMENTS. FOREIGN EXCHANGE RESERVES

WILL PROBABLY EXCEED \$7 BILLION BY THE END OF THIS FISCAL YEAR. THE DIFFICULTIES OF IMPLEMENTING ECONOMIC POLICIES AND PROGRAMS REMAIN SERIOUS AND ARE COMPOUNDED BY THE POLITICAL INFIGHTING AMONG THE JANATA PARTY'S LEADERS, BUT INDIA'S CUMBERSOME ECONOMIC SYSTEM CONTINUES TO LUMBER ALONG. END SUMMARY.

2. AGRICULTURE. AGRICULTURE. THE SOUTHWEST MONSOON HAS BEEN VERY FAVORABLE SO FAR THIS SUMMER, ALTHOUGH IT IS IMPORTANT THAT RAINS CONTINUE THROUGH SEPTEMBER. OUR PRELIMINARY ESTIMATE OF THE OUTPUT OF THE KHARIF CROP THIS FALL IS 78 MILLION MT, SLIGHTLY HIGHER THAN THE RECORD KHARIF HARVEST LAST YEAR. IT NOW APPEARS THAT FOODGRAIN PRODUCTION IN THE 1978-79 CROP YEAR WILL BE GENERALLY VERY SATISFACTORY AND COULD EXCEED LAST YEAR'S RECORD PRODUCTION OF 125 MILLION MT. THIS SITUATION WILL PUT CONTINUED PRESSURE ON THE COUNTRY'S INADEQUATE GRAIN STORAGE FACILITIES, WHICH HELD 18 MILLION MT OF WHEAT AND RICE AT END JULY 1978. THE GOI IS HOPING TO DISTRIBUTE 1.2 MILLION MT OF FOODGRAINS, MOSTLY WHEAT, FOR FOOD-FOR-WORK PROJECTS IN RURAL AREAS DURING 1978-79. ALTHOUGH THIS PROGRAM GOT OFF TO A SLOW START LAST YEAR IT HAS BEGUN TO MOVE FORWARD IN A NUMBER OF STATES. THERE MAY BE SOME FURTHER EXPORTS OF WHEAT AND RICE THIS YEAR. THE GOI HAS PUT HIGH PRIORITY ON EXPANDING LAND UNDER IRRIGATION, BUT INADEQUATE UTILIZATION OF EXISTING LIMITED OFFICIAL USE

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IRRIGATION WORKS REMAINS A PROBLEM. ALSO, MORE INSTITUTIONAL CREDIT IS GOING TO RURAL END USERS DESPITE NUMEROUS DIFFICULTIES (NEW DELHI A-159).

3. INDUSTRY. INDUSTRIAL PRODUCTION IS STILL CONSTRAINED BY THE USUAL PROBLEMS, POWER SHORTAGES, LABOR UNREST, INADEQUATE DEMAND, ETC. THE POWER SITUATION IN GENERAL HAS IMPROVED SOMEWHAT IN RECENT WEEKS; POWER GENERATION GREW BY ALMOST 15 PERCENT BETWEEN APRIL AND JULY 1978 PRIMARILY BECAUSE OF HIGHER HYDROELECTRIC OUTPUT. HOWEVER, OVERALL POWER GENERATION IS STILL ABOUT 10 PERCENT SHORT OF THE COUNTRY'S REQUIREMENTS, AND SEVERE POWER SHORTAGES IN WEST BENGAL AND BIHAR ARE DISRUPTING INDUSTRIAL PRODUCTION AND OTHER ACTIVITIES THERE. PRIVATE SECTOR INVESTMENT IN MANY INDUSTRIES STILL APPEARS SLACK TO US, DESPITE GOVERNMENT CLAIMS TO THE CONTRARY. ALTHOUGH INDUSTRY MINISTER FERNANDES CONTINUES TO TALK ABOUT ACHIEVING AN INDUSTRIAL GROWTH RATE OF 7-8 PERCENT THIS FISCAL YEAR, WE REMAIN SKEPTICAL THAT THIS TARGET CAN BE REACHED (NEW DELHI A-148).

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4. PRICES AND MONEY SUPPLY. DURING THE FIRST FOUR MONTHS OF THIS FISCAL YEAR (APRIL-JULY), WHOLESALE PRICES INCREASED BY 1.7 PERCENT. THE WHOLESALE PRICE INDEX AT THE END OF JULY 1978 WAS ACTUALLY ONE PERCENT LOWER THAN TWELVE MONTHS BEFORE, IN JUNE 1978 THE CONSUMER PRICE INDEX FOR INDUSTRIAL WORKERS HAD RISEN BY 1.9 PERCENT SINCE MARCH, BUT WAS ONLY 2.2 PERCENT HIGHER THAN IN JUNE 1977. A FAVORABLE SUPPLY SITUATION (BECAUSE OF ABUNDANT CROPS AND LIBERAL IMPORTS OF ESSENTIAL COMMODITIES) HAS BEEN THE MAJOR REASON FOR PRICE STABILITY DURING THE PAST YEAR. ON THE OTHER HAND, THE MONEY SUPPLY HAS INCREASED BY APPROXIMATELY SIX PERCENT DURING APRIL-JULY 1978 ON TOP OF THE 15 PERCENT RISE IN 1977-78. PRIME MINISTER DESAI AND FINANCE MINISTER PATEL ARE WORRIED ABOUT THE RISING MONEY SUPPLY THAT IS DUE TO THE CONTINUING FLOW OF REMITTANCES FROM INDIAN WORKERS ABROAD, INCREASED COMMERCIAL
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BANK CREDIT AND A SLOWER RATE OF GROWTH IN TIME DEPOSITS.

WE BELIEVE, HOWEVER, THAT THE GOVERNMENT HAS THE PRICE SITUATION PRETTY MUCH UNDER CONTROL BECAUSE SUPPLY FACTORS ARE MORE IMPORTANT THAN MONETARY TRENDS IN DETERMINING THE RATE OF INFLATION IN THE INDIAN ECONOMY.

5. BALANCE OF PAYMENTS. THE LARGER THAN EXPECTED TRADE DEFICIT OF AROUND \$700 MILLION IN 1977-78 WAS DUE TO GROWING IMPORTS, PARTICULARLY OF ESSENTIAL GOODS SUCH AS EDIBLE OILS AND PETROLEUM PRODUCTS, AND SLUGGISH EXPORT GROWTH (EXPECTED TO BE ONLY ABOUT FIVE PERCENT LAST YEAR). THESE TRENDS ARE APPARENTLY CONTINUING THIS FISCAL YEAR: IN APRIL-MAY THE PRELIMINARY TRADE DEFICIT AMOUNTED TO APPROXIMATELY \$50 MILLION. A 1978-79 TRADE DEFICIT ALMOST DOUBLE LAST YEAR'S DEFICIT NOW LOOKS POSSIBLE, AND FACED WITH THIS PROSPECT THE GOI HAS BEGUN TO REEMPHASIZE EXPORT PROMOTION. FOREIGN EXCHANGE EARNINGS FROM TOURISM, SHIPPING, FOREIGN SECURITIES AND, NOTABLY, INDIAN WORKERS IN THE MIDDLE EAST CONTINUE TO FLOW IN, PROBABLY AT A SLIGHTLY HIGHER PACE THAN LAST YEAR. (GROSS EARNINGS FROM INVISIBLES AMOUNTED TO ALMOST \$2.5 BILLION IN 1977-78.) AS A RESULT, THE BALANCE OF PAYMENTS SITUATION REMAINS QUITE COMFORTABLE. GROSS FOREIGN EXCHANGE RESERVES HAVE INCREASED (IN DOLLAR TERMS) BY ONLY \$340 MILLION (TO \$6.2 BILLION) DURING APRIL-JULY 1978, PRIMARILY BECAUSE OF GOI REPAYMENT OF INDIA'S LAST DEBT TO THE IMF AND THE PURCHASE OF GOLD FROM THE FUND. WE EXPECT, HOWEVER, THAT FX RESERVERS WILL EXCEED \$7 BILLION BY THE END OF THIS FISCAL YEAR.

6. COMMENT. THE POLITICAL LEADERSHIP, LARGELY PRE-OCCUPIED WITH INTERNAL DISPUTES AT THE CENTER AND IN SOME STATES, SEEMS TO BE PAYING LITTLE ATTENTION TO THE DIRECTION OF THE ECONOMY. YET THE ECONOMIC SYSTEM CONTINUES TO LUMBER LIMITED OFFICIAL USE

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ALONG RELATIVELY COMFORTABLY (FOR INDIA), DUE LARGELY TO THE GOOD MONSOONS AND THE LARGE FLOW OF REMITTANCES OVER THE LAST THREE YEARS. THE SIZE AND COMPLEXITY OF INDIA'S ECONOMY MAKES CHANGES DIFFICULT TO IMPLEMENT, AND REQUIRES EITHER CALAMITIES OR VERY STRONG MEASURES TO HAVE ANY SIGNIFICANT IMPACT. UNDER THESE CIRCUMSTANCES, THE BUREAUCRACY PLAYS A LARGER THAN NORMAL ROLE. HOWEVER, THAT GROUP IS DISINCLINED, AND LACKS THE AUTHORITY, TO MAKE THE BOLD DEPARTURES SOME BELIEVE APPROPRIATE, AND RECEIVES LITTLE DIRECTION FROM THE POLITICAL LEADERS WHO ARE THE ONLY ONES WHO CAN.

7. WHETHER THE JANATA'S ECONOMIC POLICIES ARE MAKING ANY REAL DIFFERENCE AND WILL LEAD THE ECONOMY TO A HIGHER GROWTH PATTERN IN THE LONGER RUN IS DIFFICULT TO SAY. A CRUCIAL QUESTION REMAINS THE FOLLOW THROUGH, OR LACK THEREOF,

TO ECONOMIC POLICIES. OUR IMPRESSION IS THAT THE DELIVERY
OF MANY ECONOMIC AND SOCIAL SERVICES TO THE VILLAGES CONTINUES
TO BE VERY INADEQUATE FOR A VARIETY OF REASONS, INCLUDING
INSTITUTIONAL AND SOCIAL BARRIERS, CASTE RIVALRIES, CORRUPTION
AND AN INSUFFICIENT NUMBER OF GOOD ADMINISTRATORS WHO
UNDERSTANDABLY DO NOT WANT TO LIVE IN BACKWARD RURAL AREAS.
ALSO, THE LACK OF DIRECTION FROM A DIVIDED JANATA LEADERSHIP
CONTRIBUTES TO THE FAILURE TO DELIVER ON POLICY PROMISES.
GOHEEN

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